

THE FLOATING POUND AND THE STERLING AREA

1931-1939

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CAMBRIDGE UNIVERSITY PRESS

Cambridge

London New York New Rochelle

Melbourne Sydney

Published by the Press Syndicate of the University of Cambridge
The Pitt Building, Trumpington Street, Cambridge CB2 1 RP
32 East 57th Street, New York, NY 10022, USA
296 Beaconsfield Parade, Middle Park, Melbourne 3206, Australia

© Cambridge University Press 1981

First published 1981

Printed in the United States of America
Typeset and printed by Heritage Printers, Inc., Charlotte, N. C.

Library of Congress Cataloging in Publication Data

Drummond, Ian M

The floating pound and the sterling area, 1931-1939.

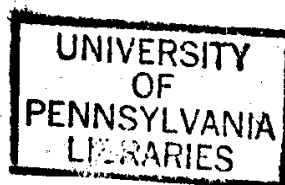
Includes bibliographical references and index.

1. Sterling area—History. 2. Foreign exchange problem — Great Britain.
I. Title.

HG255.D68 332.4'560941 80-14539

ISBN 0 521 23165 5

HG
255
D68



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Introduction: the sterling area in the 1930s

This opening chapter sketches the structure of the sterling area from the collapse of the gold standard in 1931 to the outbreak of war in 1939. It describes the chief institutions and their interactions and presents some archival evidence about attitudes and policies in the United Kingdom during the critical months of 1931-2 and at the Ottawa Conference in the summer of 1932. The material serves as an introduction to the more detailed discussion in Chapters 2 through 10.

Chapters 2 through 5 examine the routes by which India, South Africa, and Canada did or did not adhere to sterling after September 1931 and trace some aspects of the relationship between sterling and the economies of Australia and New Zealand. These chapters are meant to provide a survey of the relationship between sterling and the more important Empire currencies. In Chapters 6 and 7 we turn to the World Monetary and Economic Conference of 1933 – the London Conference that was called by the League of Nations in response to Anglo-American initiatives. Concentrating on the monetary side of the meeting, we first survey the formulation of policy in London and the defense of that policy in various international arenas, then treat the discussions with France and America before and during the conference, and finally examine the role of the Empire governments with respect to Britain's private initiatives and her public stance. Chapters 8 through 10 concentrate upon international financial diplomacy from the conference until the outbreak of war. Although they contain some material on the actual movement of rates and reserves, they are chiefly concerned with intergovernmental discussions about exchange management and exchange policy. The sterling area and the Empire retreat into the background, though from time to time they are summoned out of the wings. The final chapter is a sort of extended meditation on the significance of sterling and the sterling area during this troubled decade.

I began to study the history of sterling for several reasons. First, for

any economist who was professionally active in the 1950s and 1960s it is interesting to learn why and how the sterling area emerged during the decade when it might be said to have taken shape. Second, because in the 1970s the world has embarked on a general float of exchange rates I thought it might be interesting to know more about the last period when most exchange rates were unpegged. Third, my earlier work on Empire trade and migration had revealed the existence of an arcane subject called "empire money" and had sparked my interest in this matter. Finally, though the literature on the 1930s has been transformed in the past seven years or so, when my researches began I found it diffuse and incomplete.

At first I had seven questions in mind. Why did various countries inside and outside the British Commonwealth adhere to sterling in and after 1931? What did adherence involve? What attitude did Britain's officials take toward the emergence of a sterling area after the pound had departed from gold? What was the importance of sterling balances for the management of exchange rates and reserves? Did Britain's authorities try to manage the balances and, if so, how? Was there any sense in which the sterling area or the Empire component thereof could be said to have had a common monetary policy and, if so, what was the policy and how was it devised and kept in being? Finally, what sorts of consultations occurred within the sterling area? As I worked with the documents and the secondary literature I had to add questions. What was the intellectual basis for Britain's exchange policies and for her international monetary initiatives? To what extent can one detect "monetary interpretations" of the depression in the documents of the period itself; and how did such interpretations influence policy? Did Britain discuss or defend her own float or the sterling system in negotiations with non-sterling countries—in particular, with France and the United States? Did such negotiations have personal or political dimensions and, if so, what were they and how important were they?

At no time did I plan to explain the actual movement of the sterling exchange rate except insofar as some of the things in which I was interested were relevant to the management of that rate. Nor did I plan a heavily quantitative exercise, though I hoped to marshal such numbers as might exist. For the sorts of questions with which I was concerned rather simple approaches can extract answers from the few available numbers. For econometric exercises readers will have to look elsewhere. To master the qualitative material, I expected, would be a sufficient task. So it has proved to be. Whether the results are proportionate to the labors the reader must judge for himself.

1. *What was the sterling area?*

When we talk of a sterling area in the 1930s, what do we mean? In 1939 and for more than two decades thereafter the term has a reasonably precise meaning. The sterling area contained those countries whose foreign exchange reserves consisted wholly or chiefly of sterling. Generally they owned short-dated United Kingdom government securities or treasury bills. Their exchange rates were pegged to the pound so that the sterling area moved up and down as a single unit whenever sterling itself appreciated or depreciated. With respect to the rest of the world the sterling area maintained a common though not uniform fence of exchange controls, although within the area such controls were relatively lax or altogether absent. Foreign exchange earnings were largely pooled and held by the United Kingdom on behalf of the members. Only South Africa maintained significant gold reserves outside of the pool. There were consultations about controls, imports, capital movement, and drawings on the pool; these discussions naturally centered on the exchange control.

Before the outbreak of war in 1939 things were less tidy, and they are therefore harder to describe. There was no formal pooling of reserves, and exchange controls were almost unknown in Britain, the Empire, and the foreign countries that had adhered to sterling. Yet it was generally understood that soon after Britain had abandoned the gold standard in September 1931 a sterling area or sterling group had somehow come into existence. It included India, the Dependent Empire, some semi-independent territories such as Egypt and Iraq, a varying cast of foreign countries, and all the Dominions except Canada. As the area was not fenced about with exchange controls its members had relatively little to confer about, and it appears that they seldom did so. We may define the sterling area most precisely by asking two questions. How were exchange rates fixed? Where were reserves held?

Most of the sterling countries kept their official reserves, wholly or in part, in the form of sterling claims. Such arrangements were of very long standing. Peter Lindert has estimated that in 1913 Britain's short-term obligations to governments and central banks were at least £80 million – 250 percent of her gold reserves at that time.¹ He also claims that since before 1900 such obligations had been growing faster than reserves. Among the holders who could then be identified, much the largest were India and Japan. They pointily accounted for 75 percent of all the identifiable obligations to external governments and central banks. But 19 other holders can also be identified. Among them were Australia, New

Zealand, South Africa, Canada, and various Latin American and European states and banks. Besides these identifiable claims, Lindert reports a much larger total of unspecified claims, largely though not entirely private.

Besides these official balances commercial banks and private traders had long held working balances in the London market. Many payments had been through London banks and much finance had been raised there, while every quarter large sums were transferred from overseas debtors to British owners of overseas bonds and shares. Through the highly developed London financial market sterling could be lent out for short periods at attractive rates of interest and with little or no risk of default. As long as sterling was firmly attached to gold such sterling assets also bore no exchange risk. The transactions balances in sterling were especially important for the "imperial banks" that provided commercial and exchange banking services throughout so much of the Empire, the Far and Middle East, and Latin America; but European and American banks also maintained transactions balances in London, and so did many private traders and governments.²

During the First World War and in the 1920s, London no longer enjoyed the same unquestioned centrality in world finance. As the United States became a more important buyer, supplier, and financier, the world found it more important to hold relatively large transactions balances of dollars in New York. Nevertheless, the imperial banks and the Empire trading and financial system continued to rely chiefly on London. Further, the Empire monetary authorities were increasingly likely to hold sterling as official reserves. This tendency was increased by the growth of the currency boards, which provided most of the colonial Empire and the Middle East with currency and coin.

In the 1920s the Indian authorities continued to hold sterling along with gold and silver. The currency boards built up their holdings. So did the new South African Reserve Bank, though it still relied more on gold than on sterling. In New Zealand and Canada the monetary authorities held only gold, and the Canadian banks held only small working balances in London, relying chiefly on New York funds as secondary reserves. The New Zealand banks, however, like the Australians, operated a sterling standard whereby they held London funds, buying and selling claims on London at exchange rates agreed among themselves.³ In Australia the monetary authorities were prepared to hold sterling, although they were not always eager to do so. Outside the Empire altogether, there was a considerable buildup of official sterling balances among the Continental countries. Encouraged by the Brussels Conference of 1920 and then again by the Genoa Conference of 1922 to economize on gold by

holding foreign exchange instead, some countries built up considerable sterling holdings. The largest and most inconvenient belonged to France.

The Macmillan Committee estimated that in December 1928 Britain's net short-term sterling obligations were at least £300 million – more than four times her gold reserves.⁴ Such obligations continued to increase through 1928, but then they fell substantially in 1929–30 and disastrously in 1931. In three years the total reduction was £403 million; of this, £293 million went across the exchanges in 1931 alone.

As long as sterling was freely convertible into gold at a fixed price, sterling obligations were "as good as gold." But with the collapse of the gold standard in summer 1931, culminating with Britain's departure from gold on 21 September, this was no longer so. Sterling balances would still buy gold; sterling had not become inconvertible into other currencies; but the gold value of reserves and their international purchasing power fluctuated with the value of sterling. With the floating of the pound countries had to choose what exchange regime to adopt. Each country in principle could stay with gold, float, or stay with the pound.

A currency could be related to sterling in three ways. First and simplest was the currency board system of the colonial Empire, Egypt, Iraq, and some mandated territories such as Palestine, in which an overseas monetary authority maintained an automatic relationship between its money and sterling, mechanically issuing local currency in exchange for sterling and vice versa. Second and considerably more complex was the system of semiindependence, in which local monetary developments were not linked simply or mechanically with sterling, though the monetary authorities had pegged their moneys rigidly to sterling and held large sterling balances. This was the system of India, Australia, New Zealand, South Africa, and Portugal. Third was the autonomous system, in which the monetary authorities simply tried to maintain a reasonably steady sterling exchange rate without necessarily concentrating their reserve assets in sterling or committing themselves absolutely with respect to that rate. This was the system after 1931 in Scandinavia and after September 1936 in France.

For the currency board areas there were no questions of policy when Britain left gold. For the areas of monetary semiindependence it was necessary to decide whether to follow sterling, gold, or something else. For other countries, especially those that left gold soon after Britain, it was necessary to decide whether to follow sterling, return to gold, or follow some independent course.

In Canada the government had stumbled in 1929 to a floating dollar.

It was now to ask itself whether, for the sake of Empire solidarity, a predictably protective tariff, or both, it should peg to the pound. For India and in South Africa also, decisions had to be taken. In later chapters we examine the appropriate vacillations and uncertainties.

In Australia and New Zealand the governments did not yet control the fixing of exchange rates. At the Bank of England Governor Montagu Norman believed that the Australian treasurer had to approve the exchange rates that the banks fixed,⁵ but it is very far from clear that this was so; only after a considerable battle among the banks did the Commonwealth Bank impose an exchange rate in December 1931. As the banks had always quoted an exchange rate on sterling and sterling alone, the Commonwealth Bank did the same. It may be argued that Australia stayed with sterling due to absence of mind. According to the Commonwealth Bank's historian, it imposed its rate without the concurrence of the other banks and without consulting the government, with whom its relations were not good. Thereafter, though the Australian trading banks continued to hold London funds of their own, the Commonwealth Bank managed the rate by allowing its own London funds to rise and fall. The Bank had more or less accidentally become the holder of Australia's basic exchange reserves, both gold and sterling.⁶ In 1922-4 the Australian currency authority had considered returning to gold in advance of the United Kingdom; in 1931 its successor, the Commonwealth Bank, seemed not to have considered the matter at all.

Similarly, in New Zealand the banks had managed the exchange rate among themselves for many years. In New Zealand as in Australia and South Africa, exchange rates had long been quoted as premiums or discounts on London funds – a technique that perpetuated the illusion that a pound was a pound regardless of its location. But in 1930 the premium had begun to rise – that is, the Australian and New Zealand pounds had depreciated markedly vis-à-vis sterling. At length the New Zealand government, hoping to revive the domestic economy, imposed an exchange rate on the banks while indemnifying them against loss. This rate too was in terms of sterling; like the Australian, it endured without change for many years.⁷

Why choose sterling? India, as we shall see, was not allowed to choose anything else. For colonial currency authorities, the question could hardly have arisen. For Australia and New Zealand, in retrospect the choice seems natural enough. Britain was the chief market and the chief industrial competitor; if the exchange rate was a sterling rate, banks would not have to learn anything new and their London funds would not suffer windfall loss, whereas it would be easy to forecast the local price that any external price would imply – no small matter for governments fac-

ing a collapse of world market prices for their products. In South Africa, unlike Australia or New Zealand, there was a genuine attempt to stay with gold, and therefore the question of exchange regime was debated openly. The discussion was much influenced by the fact that Britain was South Africa's chief export market.⁸ Similar considerations must have swayed the smaller countries in Europe and Latin America that sooner or later pegged to sterling. For Canada and South Africa both situation and debate are complicated by Anglophobia.

For some parts of the Empire pegging to sterling was not a novelty. Most colonial currencies had been stabilized in this way for a very long time. Nor was it at all novel to keep one's external reserves in London. Britain's overseas banks had always done this. Their exchange transactions operated almost entirely through London, and they could not employ idle balances in the overseas territories where they operated because these territories did not have active money markets. Empire governments regularly held sterling balances because they regularly spent large amounts of sterling, especially to service their external debt. Colonial monetary authorities held sterling assets as cover for their currency issues and to manage the exchanges. As central banks were set up in the Dominions and India these new institutions also carried sterling balances for the same reasons. In the 1920s and 1930s there was some shift of sterling balances from "unofficial holders" – chiefly the overseas banks – to "official holders" – monetary authorities and central banks inside the Empire and outside it. But the sterling balances were not created in 1931. They had been there for decades. Indeed, their prior presence made it more natural for so much of the world to operate a sterling standard after 1931.

When Britain left gold Portugal at once pegged the escudo to sterling at the rate of 110 to the pound. For some time the country had been deliberately accumulating sterling reserves. On 26 September the government told the U.K. embassy, "It is certain that the majority of Portuguese interests abroad are bound to English currency and the stability of the financial reorganisation which had been undertaken in Portugal closely depends on the stability of the pound." The embassy reported that the government had £50 million in London and that there were also large private balances; hence Portugal could not regard the depreciation of sterling with equanimity. By December Montagu Norman told the Foreign Office that though he had no official information on Portuguese exchange policy he believed that Portugal was "content to stabilise on sterling as long as the pound does not depreciate beyond a certain point, which for the time being has been fixed at \$3.32."⁹ That is, if sterling were to fall below \$3.32 the Portuguese would think again. If Norman

is to be believed, the Bank of England was not in close contact with the Portuguese monetary authorities, and there is nothing in the Foreign Office records to suggest any sort of liaison. It appears, therefore, that Portugal stabilized on sterling because it was trapped; its sterling balances were so large that it could not bear the capital loss that any other policy would have entailed.

In Scandinavia the development was more complex. Denmark, Sweden, Norway, and Finland all followed sterling off gold. But none pegged to sterling at once, and both Finland and Denmark experimented with exchange controls both before and after their departure from gold.

On 6 October 1931 the Bank of Finland acquired a monopoly of dealings in foreign exchange, fixing a daily rate for transactions in sterling. Exchange control was introduced, and the country tried unsuccessfully to borrow abroad. These efforts were not sufficient, and confidence was not restored. Hence on 12 October the Bank of Finland announced that it would apply for permission to end the gold convertibility of its paper currency. Thereafter there was a severe "valuta crisis" – restrictions and prohibitions on the delivery of foreign exchange. British traders complained that they could not get payment for exports; the Foreign Office transmitted these complaints to the Finnish government. By 31 November the Bank of Finland was following sterling, but to do so it was employing a stringent exchange control. A black market quickly appeared. On 17 December the embassy learned that the Bank of England had offered its Finnish counterpart a credit of £500,000 for four months; almost at once the finmark was freed to find its own level as the exchange controls were dismantled.¹⁰

Among the Scandinavian countries things were somewhat confused. Denmark left gold in a sort of two-stage shuffle. On 23 September the export of gold was banned, but it was still possible to convert notes into gold bars. At once the public began to present notes for conversion; at the same time the agricultural interests wanted the country to leave gold altogether. In Sweden the authorities were trying without success to raise a French loan for the defense of the gold standard. In Norway too the central bank was most reluctant to leave gold, but when the Bank of Sweden learned that it could not raise a loan on acceptable terms, on 27 September it convened a meeting with central bankers from Denmark and Norway. Immediately thereafter Sweden banned gold export and ended gold convertibility, Denmark also ended the convertibility of notes into gold, and the Norwegian central bank, with deep misgivings, followed Sweden's example.¹¹ Both in Sweden and in Norway there were strong reasons for depreciation; many export contracts were denominated in sterling, and these were often long-term obligations. Den-

mark found its principal export market in the United Kingdom. Hence the British debacle had at once generated speculative pressures that the three central banks could not withstand unaided. The Danes had been obliged to introduce exchange controls. Even after leaving gold they could not at once dismantle them. In all three countries the process of adhering to sterling was an extremely gradual and imperfect one. Although central banks would quote sterling exchange rates, these rates were by no means stable; during the winter of 1931-2 it was said in Whitehall that Scandinavia followed sterling "as far as possible." By January 1932 Venezuela, Bolivia, and Japan had joined the group of independent countries that were basing themselves on sterling or gravitating that way.¹²

In the documents there is remarkably little sign of intergovernmental discussion with respect to these currency developments. The Treasury was actively opposed to any such discussion, and when the Foreign Office accidentally suggested to the Danish, Swedish, and Norwegian governments that they should cooperate with His Majesty's government the Treasury insisted on a retraction. The central banks could and should cooperate with the Bank of England; the governments could not cooperate and should not. In 1935 S. D. Waley of the Treasury wrote to F. Ashton Gwatkin of the Foreign Office, remarking that His Majesty's representatives "should hold studiously aloof from any devaluation controversy so that no country can later claim they stayed on gold or left gold as a result of suggestions from this side." Nor could Britain safely urge countries to join the sterling area either by pegging to sterling or by holding sterling balances. Countries were welcome to peg to sterling, but the decision had to be theirs. As a Bank official later wrote, "We here do not encourage any country to join the sterling bloc or indeed to devalue in any way; our attitude has always been that each country must decide this question for itself."¹³ The Treasury view had long been the same, as the Foreign Office was told when from time to time it asked for guidance. The reasons are not clearly explained, but one can easily guess at them. If the Bank or the Treasury were to urge an overseas government to peg to sterling, they could hardly avoid some responsibility for the security and convertibility of the results. Further, exchange policy was political dynamite inside the Empire and outside it. The U.K. authorities could hardly appear to take sides in such controversies. For India and the Dependent Empire, of course, the case was different. As London was ultimately responsible for their good government, they could not be allowed to pursue incorrect policies. As we shall see in Chapter 2, India's officials had to be taught this lesson in 1931. On the other hand, this experience had itself taught a lesson to Bank and

Treasury. If a dependency could demand a £100 million credit to support its exchange position, what might not a Dominion or a foreign state expect?

There were, however, certain encouragements that Britain could give. In December 1931 the central banks of Denmark and Finland applied "urgently" for credit from the Bank of England. Denmark wanted £250,000, and Finland £500,000. These were needed to increase resources so as "to maintain the sterling basis." The Bank would not grant the credit without governmental approval. In the Treasury Sir Richard Hopkins was very much in favor of such credits. He wrote:

One of the leading objectives that we ought to have in mind as soon as we can keep sterling steady at a reasonable level, is to make it easy for as many as possible of the unstable currencies to base themselves on sterling so that we may become the leaders of a sterling block which, pending our restabilisation on gold, would have the best opportunities of mutual trade and would give sterling a new force in the world. The natural leading components of such a sterling block are first of all the various parts of the Empire and secondly the Scandinavian countries. If we have this sort of objective in view I think the Bank of England ought to be ready to give assistance to countries which are following us when the assistance asked is within our compass. . . . This may perhaps be regarded as a first step upon a long road, the end of which cannot be foreseen. On the other hand we need go no further down it than we wish, as it seems to me, the road leads in the right direction.¹⁴

Neville Chamberlain, the chancellor of the exchequer, approved, and the loans were extended. The sums were small relative to the amount that Britain had committed and would commit to Australia and New Zealand. But they were enough to dissolve some of the exchange controls in the Nordic zone and to ensure that Nordic currencies would float less wildly than in the autumn of 1931.

Already in 1930 the Bank had provided sterling so that the New Zealand government could meet its external obligations.¹⁵ Australia too was allowed a credit in 1930 when its overseas funds were alarmingly insufficient but before the Commonwealth Bank had undertaken to manage the Australian exchanges.¹⁶ Later drawing rights were arranged from time to time. As Professor Giblin has explained,¹⁷ each such drawing right was connected with Australian nervousness about London balances and with an Australian commitment that the Australian pound would not be further depreciated. The Commonwealth Bank took over the management of the exchange in December 1931 when it imposed a rate on the other trading banks. Thereafter it was obligated to buy and sell sterling freely at a price of £1.25 Australian. By mid-1932 it doubted if it had enough sterling to maintain that rate through the year. Accord-

ingly, in July it sought help from the Bank of England, asking and obtaining a drawing credit of £3 million. In July 1936 the Bank was asked for another such credit of up to £5 million so as to stave off a further depreciation. In 1937 another credit of £3 million was arranged in London, largely for defense needs. In mid-1939 the directors of the Commonwealth Bank were considering a further approach to the Bank. In fact, none of these credits was actually used, but their extension shows how anxious Norman was to maintain stable exchange rates within the sterling area.

In managing Britain's long-term lending the authorities did not ignore the effect of lending on exchange stability. Believing that in the 1920s Britain had overdone both her long-term lending and her short-term borrowing, they wanted to control the volume of new long-term overseas lending. Informal controls had existed before September 1931; they then became more systematic. The controls of the 1920s had treated the Empire preferentially, and in the new regime Empire borrowers were soon largely exempted. Norman, we know, hoped that Britain would continue to provide the Dominions with new long-term capital,¹⁸ and he spent an immense amount of time on Empire flotations.¹⁹ Such new loans could be raised and old loans converted only with the authorities' permission and in accordance with their scheduling. The Treasury described the position as follows:

Under the Chancellor of the Exchequer's request of 1 October 1932 no issue ranking as a trustee security can be made in London without prior agreement with the Bank of England regarding the amount and date of issue . . . Further, under the same request the optional replacement of existing issues by new issues involving new underwriting or an invitation of the public to subscribe new cash is made dependent upon the express approval of the Chancellor. The object of these requests is to co-ordinate the requests of intending borrowers and so to prevent possible congestion and depression of the market, and their value has been abundantly proved by recent experience.²⁰

But in giving permission it was necessary to consider the position of the would-be borrowers. In the early 1930s there was real risk of Australian default, and Norman wanted Britain to be a patient creditor. Hence, in due course Australia was allowed and helped to convert overseas debt to the lower interest rates that ruled in the 1930s. In 1939 Norman arranged for the refinancing of a large New Zealand maturity. The terms were stiff, but the alternative was either default or depreciation.²¹

It was hard to ensure a rationally metered flow of new sterling when subordinate governments could borrow in London or when conversion loans might be floated in London for the repayment of nonsterling obligations, especially in the United States. As Australasian trade and debt

were so firmly based on Britain, there was little risk that credits would at once lead into a demand for dollars or other foreign moneys. In Australia the Commonwealth government coordinated the borrowing of the states and floated loans on their behalf. But Canada was extremely worrying. The senior Dominion had nothing like the Australian Loan Council; its provinces could and did borrow as and when they liked. Further, its great cities floated loans of their own. By 1930 its provinces and cities were as indebted to American financiers as to British. Hence there was a considerable risk that they would try to borrow in London at the low interest rates of the 1930s so as to repay old and more expensive credits in the United States. Also, if any Canadian entity were to borrow heavily in London the dollar-sterling exchanges could at once be disturbed. Canada was not a member of the sterling area; neither government nor banks held significant sterling balances; in the absence of special arrangements a sterling loan would at once be transferred into dollars, depressing the exchanges or depleting Britain's reserves. Finally, the Treasury believed correctly that many Canadian municipalities and some Canadian provinces were bad risks, and it also suspected that some American firms might try to borrow in London through their Canadian subsidiaries.²² Hence there was some effort at informal control. In 1933, when in London for the World Monetary and Economic Conference, Prime Minister R. B. Bennett promised the Bank that the Dominion would be the only Canadian borrower on the London market;²³ but this was a gentlemen's agreement only, and when Bennett left office in 1935 it lapsed. In 1936 Norman and the Treasury pressed for a new understanding that would exclude the provinces and the municipalities while admitting the smaller mining and industrial issuers. The new Canadian cabinet would not make any such promise, but the minister of finance told Norman that if the Bank refused permission Canada would not object.²⁴

With respect to Empire demands for long-term finance, Sir Henry Clay tells us that Norman "exercised a banker's right to criticise."²⁵ At times he may have done more. To support the exchanges and to get sterling for their home charges the Indian authorities could and did borrow at large in the City, where short-term India bonds were well known and understood. But during its troubles of 1931-2 the South African government had not found it easy to borrow at large either in London or elsewhere. Further, when New Zealand's reserves were dwindling rapidly in 1938-9 neither Norman nor the City was at first inclined to be helpful. From time to time, as in mid-1931, even India could find the market unreceptive. At such times would-be borrowers were inclined to suspect that the Bank had told the mar-

ket to be unreceptive. It is impossible to prove that such things never happened and tempting to believe that they sometimes did. A further difficulty was that Norman himself was often the intermediary between the would-be Empire borrower and the market. The governor could and did say that some issue was impossible because the market would not provide the funds. In Chapter 5 we shall see examples. But how did he know? Was he always right? Could he always give technical advice only, ignoring his feelings about the borrower's policies?

By managing Britain's lending, both long-term and short, the U.K. authorities could do a good deal to foster exchange stability within the sterling area and to discourage exchange controls. In principle they might also have done something by cooperating with other central banks. As far as Europe was concerned this was possible; in the Empire it was much more difficult.

When sterling left gold in September 1931, the Empire was not well endowed with monetary expertise or even with central banks. As the outer Empire countries equipped themselves with central banks and as those new institutions were staffed so extensively from London, it was natural to suspect that Britain was equipping the Empire with monetary institutions that the Bank of England could somehow control. The Reserve Bank of South Africa had been set up in 1921. Its first governor came from the Bank of England. Only in 1934-5 were central banks established in Canada, India, and New Zealand. The Bank of England provided a deputy governor for the Bank of Canada and a governor for the Reserve Bank of New Zealand; Montagu Norman selected the first governor of the Reserve Bank of India. In 1930 the Bank's advice had been sought on the Australian financial crisis and on New Zealand banking law. Sir Otto Niemeyer made an expedition to the Antipodes. New Zealand's reserve bank law was largely based on his recommendations. Lord Macmillan presided over the Canadian Royal Commission that recommended a central bank for the senior Dominion. All these new central banks were "shareholder institutions," modeled more or less closely on the Bank of England itself. In Australia the suggestions of Sir Ernest Harvey had helped the Commonwealth Bank to evolve into a proper central bank.

Norman's biographer has explained that though the governor took an active interest in the development of Empire central banks he did not want to run them or try to do so. Nevertheless, through correspondence and visiting he made a determined effort to keep in touch with their governors. Professor Sayers has given us more information about Norman's efforts and concerns with respect to Empire central banking.²⁶ Norman's activity reflected several interests. In the Empire as on the

European continent he wanted to spread the gospel of central banking, and he hoped that the new banks would stand in proper independence of government – hence his labors to disseminate a code of central banking practice. This labor was not inappropriate. Everywhere in the overseas Empire there was confusion about what central banks were, were for, or could achieve. Norman also wanted to make sure that the new banks were properly run. Finally, his concern with these matters cannot have been divorced from his hopes with respect to sterling after September 1931. The better managed the Empire monetary and currency regime, the greater the chance that exchange rates would remain reasonably stable at least within the Empire, and the larger the likelihood that sterling and the sterling bill would retain their importance in world trade and finance.

2. Empire money and the sterling bloc

The idea of a sterling bloc could easily become entangled with the idea of an Empire bloc. Indeed, in the winter of 1931-2 it was hard to keep the two ideas distinct, even though Canada and Hong Kong were not on sterling and Egypt, Iraq, Portugal, and the four Nordic countries were – at least, more or less. During the autumn of 1931 the City contained a good deal of sentiment in favor of some sort of sterling bloc, and the Empire money enthusiasts, knowing that an Imperial Economic Conference would soon convene at Ottawa, elaborated their schemes with increasing fervor. Inevitably therefore, the Bank and the Treasury officials had to concern themselves about the sterling area while worrying about a sterling policy, war debts, reparations, and all the manifold perplexities of that complicated and discouraging winter. It is now well known that the authorities began to manage sterling and to worry about the correct sterling-dollar exchange rate almost as soon as they had abandoned gold. Professor Sayers and Dr. Howson have traced the adventures of Bank and Treasury from September 1931 through summer 1932. The authorities quickly convinced themselves that they could not at once peg the pound or return at once to gold. They also came to believe that the pound should be kept below the old par of \$4.86 2/3, but for some time they were skeptical about their power to peg sterling at any particular level. London's external liabilities were still immense and her gold reserves still exiguous.¹

The Dominions and India were intensely interested in the price of sterling because it directly affected the prices in domestic currency of the things they bought and sold outside the sterling area. When South Africa and India inquired about exchange policy they were rebuffed.

To J. H. Thomas, the Dominions secretary, and his staff the question was of importance. They would have to deal with the Dominions' importunities, and they recognized the interconnections between exchange rates and tariff bargaining. They could less easily be ignored. In the Treasury, though perhaps not in the Bank, the authorities were at one with the Empire on one question: wholesale prices were clearly too low, and recovery depended on a reversal of the price decline that had pushed some debtors, private and governmental, to the brink of default or over that precipice. The authorities certainly did not and could not place Empire questions in the foreground, but in formulating exchange policy they could not ignore and did not ignore the question of the sterling area. To them it was closely connected with the question of confidence. If sterling were rationally managed people would have confidence in it and adhere to it. Further, and equally important, they would hold sterling balances. But confidence also depended on the avoidance of inflation and therefore on the balance of the government budget. Sterling therefore was still dependent on fiscal rectitude, and so was the sterling area. Later in the decade the authorities would read similar sermons to the French. For the time being it was most important to read them to one another and to their political masters. The outside world, too, should be reassured by emollient pronouncements.

In October 1931, from the Treasury, a senior official explained,

The countries that have been driven off the gold standard with us may become the nucleus of a new block. If we can manage our devaluation in an orderly fashion – and only on that condition – then leadership of the block will be ours and we may be able to maintain to a large extent the prestige of sterling and the vital commercial business which it carries with it. In that case force of circumstances must bring some accommodation with the gold standard countries. But the key to that future is less a present study of future policy than a resolute handling of the problems of today.²

Soon thereafter the Treasury officials were set to work on the question of Empire money. The Federation of British Industries and the Empire Economic Union had produced a joint report that advocated among other things stabilization of intrainperial exchange rates and a common Empire currency. Eventually, early in March 1932 the Cabinet received a Treasury memorandum on the subject. Though this memorandum seems to have been lost, its contents can be reconstructed from the surviving drafts. The principal authors seem to have been Sir Richard Hopkins and Sir Frederick Phillips of the Treasury.³ One official explained, "The object to be aimed at is an Imperial Sterling standard, which . . . should include as many foreign countries as possible." But sterling could be a satisfactory standard only if Britain itself had "some definite mon-

etary policy . . . an intention of stabilizing the internal purchasing power of the pound." Another official explained that a sterling standard, preferably at par, would be highly desirable for the Empire:

There is no reason why the British Government should not definitely adopt a sterling basis for the currencies of the Empire as an object of policy and invite the Dominions to concur in it. A very large part of the business of London as a financial centre consists of the business of the British Empire, and the employment of sterling as the basis of all the currencies of the Empire would be a long step towards making sterling an effective rival of gold.⁴

At the time another official, S. D. Waley, was reminding himself that the Dominions were independent monetary authorities for which the currency board system was not appropriate. However, in 1923 the Imperial Economic Conference had recommended that the various Empire countries should set up central banks and hold sterling reserves for stabilizing the exchanges. These things were still appropriate. Further,

It would clearly be desirable from many points of view that the Dominion currencies should be linked with sterling during the period that must elapse before we can return to the gold standard. This depends of course upon the decision of the various Dominion governments. If we can succeed, as we hope to do, in maintaining the pound at a relatively stable level, and in avoiding further depreciation, it may be hoped that Canada and South Africa will recognise that it is in their interests to relink their currencies to sterling.⁵

By spring 1932 the Treasury had concluded:

The object to be aimed at should be an Empire Sterling Standard which would be as nearly as possible universal within the Empire. It involves on the part of each participating Dominion or Colony the acceptance of the policy of keeping its currency at par with sterling. It does not entitle the Dominion or Colony to claim to participate in the decisions upon which the level of sterling is varied or maintained, for the moment that claim is made the proposal passes into the realm of an Empire Federal System and therefore into the realm of impracticability. The Mother Country cannot do more, nor can she do less, than to agree in general principle that subject to her own overriding necessities the interests of the Empire would at all times be borne in mind in the framing of general policy. Within these limits there is room for fruitful discussion at Ottawa . . . The Treasury suggest that after discussion at Ottawa in which the objective would be declared, and its general colour defined, the block would be best left to grow. A sane management of sterling would do more than many conferences to secure the object in view.⁶

Meanwhile, in September 1931 Prime Minister Ramsay MacDonald had convened his own Advisory Committee on Financial Questions. Originally this committee had six members – R. H. Brand, Sir Walter Layton, Reginald McKenna, Lord Macmillan, Sir Josiah Stamp, and

H. D. Henderson. Later in the autumn John Maynard Keynes and Sir Arthur Salter joined the group. In its own work the Treasury was aware of the committee's preliminary suggestions. In March 1932, now a committee on the Economic Advisory Council, the group produced a report whose conclusions were much like the Treasury's. The members thought it would be "very desirable" if the countries that had left gold could be encouraged to link themselves closely to sterling. "By this means," they wrote, "trade secures the advantage of stable foreign exchange within the sterling area; the utility of the sterling bill as an instrument of international commerce is enhanced; and sterling itself acquires a greater measure of stability relative to gold standard countries." However, there could be no real centralization of control on an international basis because no one wanted an international central bank either for the Empire or for the world sterling area. "There remains only one form which the pursuits of a common policy can take, namely, that the Bank of England should control the value of sterling independently by the same means that it employs today; and that the other countries should so regulate their monetary systems as to maintain their exchanges at a fixed parity with sterling. This, however, is the practice that prevails today, in so far as other countries adhere at all closely to sterling." Britain could consolidate a sterling group only by convincing other countries, inside or outside the Empire, that "the closest and most definite adherence to sterling is likely to be in their best interests." This adherence depended on confidence, which in turn depended partly on international consultation. British authorities should keep in touch informally and naturally with the authorities of the other sterling countries. But little could be expected from a formal discussion, at the coming Ottawa Conference or elsewhere. Meanwhile, it would be useful if Britain could again lend overseas as long as the borrowers would spend the proceeds in the United Kingdom.⁷

This committee reported because the prime minister asked them to think about the sterling area and the Empire; the Treasury worried about these matters partly because in response to the suggestions of industrialists and Empire visionaries Chamberlain asked them to do so,⁸ partly because such ideas were in the air, and partly because J. H. Thomas, the Dominions secretary, was pressing the chancellor. Early in January 1932 he asked Chamberlain about monetary policy at Ottawa. He or his officials wrote:

I am of course well aware of the danger and difficulties of any proposals for anything like a common monetary policy within the Empire. On the other hand, disparities between exchange . . . may obviously be of even greater significance . . . than tariffs. The question, difficult as it is, can hardly be avoided.⁹

He feared Canada would raise the question of silver and asked what Britain should now do to define its policy in case any of the other Ottawa participants want to talk about money, credit, and the exchange.

Partly because his officials were at work on the question already, Chamberlain did not answer in haste; on 3 March Thomas was obliged to write again. Rather plaintively he asked, "Are you yet in a position to say anything further regarding the question of monetary policy (including silver) at the Ottawa Conference, about which I wrote you on January 4?" Chamberlain responded, "I hope to be in a position to let you have something about monetary policy and the Ottawa Conference fairly soon." Thomas hoped that the Cabinet Committee on Ottawa would discuss the matter, but its records do not reveal if it ever did so. It is known that the Treasury view was circulated, however; presumably the Treasury argument disposed of the question.¹⁰

Governor Norman was eager for "real, effective, and permanent monetary cooperation" within the Empire, but he did not think Ottawa would be the right place to discuss monetary questions. The Bank had little interest in a new form of "empire currency." It looked to the gold standard in the end, and for the time being it hoped "by all possible means [to] defend the continued validity of sterling and the sterling bill as an instrument of international exchange."¹¹

In essentials the Bank and Treasury positions were identical. It was desirable to have sterling used as a means of exchange, a unit of account, and a store of value, in international trade and finance, both inside the Empire and outside. If managed sensibly it would be used in this way. If we are to judge from his actions Norman was willing to go a step further. Once a country had decided to stabilize on sterling the Bank would extend modest credits to prevent any adventitious change in an exchange rate. As long as a government was managing its domestic affairs with circumspection the Bank would provide temporary sterling finance for that government's London obligations. But if domestic budgets were unbalanced deliberately, or if domestic credit expanded recklessly, the erring government could not count on help from London — as the New Zealand authorities discovered to their cost in 1938-9.

Outside Whitehall there was considerable interest in the expansion of the sterling area, and in the fixing of exchange rates within it. There was still a tendency to think that a pound was a pound whether it was a New Zealand or a South African pound or a United Kingdom one. Hence it seemed unnatural for the Australian and New Zealand pounds to be worth less than a United Kingdom pound. And it seemed even more unnatural to change the exchange rates within the sterling area. Because of these assumptions and because before 1931 many financial

arrangements had been made in terms of "pounds" *simpliciter*, intra-imperial changes could be inconvenient to traders, pensioners, creditors, and debtors. Furthermore, there was a widespread assumption that a big sterling area was somehow a good thing for Britain. The visionaries of imperialism were inclined to see the sterling area as a symbol of Britain's predominance and of Empire unity. It was divisive to increase intra-imperial tariffs; it was also divisive to change intrainperial exchange rates.

Leo Amery was out of office, but he had considerable influence with the Empire Economic Union (EEU) and the Federation of British Industries (FBI). It appears that it was Amery who inspired the EEU and FBI to propose an imperial currency system. He also presided over the Iraq Currency Board, and to the would-be welder of monetary unity the currency board was an ideal device. Foreign exchange reserves were held not in gold or foreign moneys but in sterling; the local supply of currency was determined automatically on the basis of these sterling reserves; because one could not change the exchange rate without at once altering the domestic currency supply, that exchange rate was almost immutable. In 1932 Amery urged R. B. Bennett to give Canada this excellent British invention; in 1933 he urged Chamberlain to do something similar for the whole Empire.

The chancellor was not impressed. He responded:

With regard to the Imperial Sterling area, I cannot see what advantage you think would accrue by your proposal even if it were practicable . . . the interests of the Dominions and of the Mother Country might not exactly harmonize on all occasions. If, therefore, New Zealand had been tied to a value of the pound fixed by Great Britain in the interests of Great Britain surely this would have led to friction and not to unity with New Zealand. I think it is much better to go on as we are doing, gradually building up world confidence in sterling, which, by degrees, is bringing one country after another into line, without any compulsion. There is another thing, which I don't think you quite appreciate at its true value, and that is the psychology of the European countries with respect to gold. If they thought that we had decided permanently to divorce ourselves from gold, I doubt very much whether they would approve, as gold still seems to them the one stable and satisfactory measure of value, though, of course, they realize that something has gone wrong with the use of it. The more I see of this difficult and complicated question, the more I am convinced that it would be wrong to lay down rigid rules in conformity with theoretical considerations. There are too many factors in the case which do not lend themselves to theory.¹²

With respect to the attitudes of the gold countries the events of summer 1933 had confirmed the chancellor in his beliefs; with respect to the

size of the sterling area and Britain's place in it the events of 1933-6 did nothing to change his mind.

At times the authorities and advisers worried about the future of the sterling bill.¹³ It was feared that if sterling floated financial business would leave London because the sterling bill of exchange, which still financed so much of world trade, would be an unstable instrument relative to other moneys. Overseas importers and exporters would be reluctant or altogether unwilling to invoice or finance in sterling because final costs and payoffs would, in terms of their own currencies, be uncertain. In the City there were discount houses and acceptance firms whose livelihood seemed to depend on the continued existence and activity of the sterling bill; if the value of sterling finance were to fall substantially these firms might starve to death. Further, there was known to be a connection between the bill market and the sterling balances. Overseas firms held sterling for placement in the market and as transactions balances to finance and support their own activities as borrowers and lenders in that market. If the market were to contract one might suppose that these balances would fall, and fall sharply. Thus the capital account of the nation would suffer no less than the profit and loss accounts of the City.

In the event, these worries proved excessive. Certainly the bill market did contract, and the specialist firms did have trouble.¹⁴ For this there were many reasons; among the more important were changes in the pattern of international payment and the fall in the volume and value of world trade. But the sterling bill and the sterling balances linked therewith did not vanish from the scene. Even when the pound was at its most unstable, as in the winter of 1931-2, many foreigners found that there was still no substitute for London. The market in forward sterling, which had existed before September 1931, developed much more quickly than some observers had expected. Through the market, therefore, exchange risks could be reduced, shifted, or altogether avoided. From late 1933 until mid-1938 sterling did not fluctuate very much, and so the actual risks were smaller than had been foreseen in the winter of 1931-2. Finally the sterling area itself, where exchange rates changed seldom or not at all, covered a very large proportion of the external trade that had financed itself through London before September 1931.

In the Foreign Office the sterling area was always regarded with unease. Until January 1932 the FO contained no specialist on economic affairs and so the unease was muted. Thereafter it was somewhat easier for the unease to be expressed, and presumably through informal channels it reached the Treasury and the Bank. However, the monetary authorities did not ask the opinion of the Foreign Office, which spluttered

along by itself. Naturally it was concerned about the way in which a sterling bloc might affect international relations. France and the United States were especially worrying to the Foreign Office, but from time to time Germany also attracted its nervous glances.

Early in 1933 Sir William Selby and F. Ashton Gwatkin of the Foreign Office prepared a memorandum on the future of a sterling group. They discussed the suggestion for stabilizing exchange rates within the bloc and then reflation so as to raise sterling prices. Such ideas had often been canvassed, and they were especially noticeable in the winter of 1932-3. Britain and the Empire were preparing for the World Monetary and Economic Conference; the Scandinavian states had asked to be informed and perhaps consulted about Britain's plan for the conference. Selby and Gwatkin thought that it would be unsafe to reflate the sterling bloc in isolation because the gold bloc would not tolerate the forcing of Britain's exports through currency depreciation. Therefore the United Kingdom would shortly be unable to import except from within the sterling bloc. They also feared that Britain might lose the bill business of the nonsterling world. Further, they thought it politically unsatisfactory to envisage any such solution without France and the United States. They wrote,

Politically, every consideration points to our not attempting to move towards a sterling bloc as an end and aim of our policy, while economically there may equally be reasons – and strong reasons – why we should not push our position as the centre of a sterling bloc too far . . . both our political and our economic interests lead in the direction of an international rather than a sectional solution.¹⁵

Another official minuted his agreement: "Even if such a sterling policy would work, which is uncertain, it would be 'disastrous politically'."¹⁶ Summarizing these and other comments, Sir Robert Vansittart, the permanent undersecretary of the Foreign Office, observed that if the World Conference were to fail Britain might be driven into a sterling bloc but more likely would have to rearm and form an alliance with France so as to control Germany, while conciliating the United States. He asked, "How would that square with a sterling bloc? Ill, I should say." Nevertheless, "the question anyhow seems to be at present rather a remote one. If matters begin to mend we shall not come to that pass; and if all goes amiss events are not likely to work out in that direction but in an opposite and worse one."¹⁷

On the other hand, even in the Foreign Office it was sometimes suggested that the sterling bloc might be a good weapon with which to frighten the gold countries into reasonableness, especially in relation to the maldistribution of the world's gold.¹⁸ It was also suggested that if

Europe were to collapse and crash into financial chaos a sterling bloc might "prove an invaluable rock to which not only we and the Dominions and other countries might cling, but at which the remaining gold standard countries, which are largely responsible for existing conditions, might also catch and thereby save themselves from destruction."¹⁹ Exactly how this salvation would be effected the writer of the minute did not explain. To Keynes the case for a sterling bloc was largely of this sort. He hoped that such a bloc would manage its currency in a rational way, first raising and then stabilizing the price level so as to assist the economic recovery not only of Britain and the Empire but of the world. Keynes assumed that the Bank of England and bloc would operate whatever monetary policy he thought sensible at the moment.

The trouble was that the sterling area generated expectations either excessively optimistic or positively dangerous.

In the early 1930s monetary nostrums were legion. Some but not all had been brewed by Keynes. To influential public men in India, Australia, and New Zealand, as in the United States, monetary expansion was to bring salvation. And imperial visionaries yearned for some visible articulation of imperial unity in the monetary sphere. These themes and pressures interacted. Politically and diplomatically they were important. Even if its monetary authorities had been minded to experiment Britain could not safely have done anything too terribly visionary: foreigners held very large sterling balances, and from late 1931 the Bank kept itself regularly informed about these alarming obligations. The balances generated a fear that was the main obstacle to Keynes's more visionary schemes for commodity money and managed currency. It was bad enough to be off gold; if the balances were not to drain away and depreciate the pound to an unacceptable extent it was essential to be orthodox and especially noninflationary, no matter how much one might want prices to rise. Credit could become easy and cheap so long as the new credit did not finance government deficits, and so long as the budget stayed balanced. Thus foreign confidence could be retained and the sterling balances kept in London.

From the winter of 1931-2 until the end of the decade the Treasury was constantly on guard lest the overseas sterling countries, especially the Empire countries, should undermine confidence in sterling by foisting or trying to foist experimental programs – deliberate credit expansion, deficit budgeting, public works programs – onto the United Kingdom. The Treasury officials also guarded against the idea that the administration of sterling might somehow be internationalized. In an Age of Conferences such an idea was natural enough, and it was sometimes suggested by those who should have known better, such as Keynes.

In November 1931 Keynes circulated a paper proposing an Empire Monetary Conference that would decide how sterling should be managed in future. By fixing "broad outlines of an Empire Sterling Standard" the United Kingdom "could then approach other countries in a vastly stronger position," and "South America, Central America, and Scandinavia might eventually go in a sterling standard, managed by the Bank of England and pivoted on London."²⁰ There were, Keynes observed, three ways to manage sterling, and the conference ought to consider all of them. The pound might go back to gold at some new, presumably lower, but definitive parity. It might simply be managed by the Bank with no definite commitments. It might be managed so as to stabilize sterling prices – the alternative that Keynes himself favored.²¹ Fortunately for everyone this suggestion died almost at once. But when MacDonald's committee of worthies reported early in March 1932 Keynes's suggestions had been discarded, consigned to the same wastepaper basket that was to receive so many schemes for Empire monetary solidarity.²²

3. Empire money at the Ottawa Conference

Meanwhile, Leo Amery was doing his best to excite trouble on the monetary front. For years he had been concerned about Empire money. In the early twenties he had espoused schemes of Empire exchange and credit, which had won him nothing but the contempt of the Treasury officials. Late in January 1932, Amery wrote to Prime Minister R. B. Bennett of Canada, "I trust you will not let the Treasury here veto the fullest discussion at Ottawa of the currency question."¹

Late in February the Canadian House of Commons resolved that the Canadian government should "initiate and support measures for the stabilisation of the currencies of all British countries." Hence nobody was surprised when Bennett told Sir William Clark, the U.K. high commissioner, that the conference should emphasize currency as well as trade.²

Chamberlain decided that he wanted to know in what form the Canadians would raise the question of currency.³ Clark thought that the Canadians had nothing concrete in mind, but Thomas asked him to find out for certain.⁴

For more than two months there was no word from Ottawa. In mid-April Bennett told Chamberlain he expected the United Kingdom delegation would make the most important contribution.⁵ At the same time the government of India weighed into the lists. Delhi supported Canada's idea of a discussion of "fundamental issues of whether there could be a concerted currency policy among the Empire countries." It

hoped Britain would accept "the principle that sterling policy shall be regulated with the deliberate purpose of producing a certain level of prices," taking account of Empire countries' interests.⁶

This was more than the Treasury could stand. Later that month its officials wrote that it was impracticable for Britain to admit the Dominions to the management of sterling. The coming conference was not likely to say anything definite about sterling management, and so "the outcome of the discussion on currency policy at Ottawa is likely to be somewhat negative."⁷

At long last, late in May the Canadian prime minister cabled his draft conference agenda to London. He said:

The Canadian Government . . . are convinced that measures for the development of inter-Imperial trade must, to a considerable degree, be dependent upon the stabilization at appropriate levels of our several currencies. It is recognised that in some respects these questions will not admit of satisfactory settlement on exclusively Imperial lines. The Canadian Government accordingly, feel it would be premature to proceed with detailed plans for concerted action in this field until it is clear as to the policy which will be adopted at the forthcoming conference in Lausanne.⁸

In the agenda, under "Monetary-Financial Questions" he included: "Consideration of desirability and feasibility of taking steps to restore the general price level and to stabilize exchange, including consideration of monetary standards." The Canadian authorities thought it vital to stabilize exchange rates, though as yet they had nothing special to propose.⁹

Following the usual practice for imperial conferences, Bennett repeated his telegram to the other Dominions. In response the New Zealand government urged that the agenda papers should include "currency and price level, central banks, and kindred problems." It feared that the United Kingdom would omit or ignore these matters.¹⁰

Whitehall was not happy with the Canadian suggestion for the agenda. It replied that it would prefer the following words: "consideration of existing interrelationships of various currencies and monetary standards of the Empire and of means to be taken to promote secure exchange conditions most favourable to mutual trade." And it commented: "We . . . are of opinion that favourable conditions for framing any definite plan of stabilisation may be found not yet to exist."¹¹ The Canadians insisted that they wanted to fix "wider terms" than the British wording would allow. They demanded and got the following: "Consideration of existing interrelationships of the various currencies and monetary standards of the Empire, and of the desirability and feasibility of taking

steps to restore and stabilise the general price level and to stabilise exchange."¹²

Once the agenda was settled the Treasury prepared another memorandum that was in effect a comment upon it. The arguments were the same as before. It would be a good thing if prices were to rise. But monetary manipulation alone would not raise them. It would be premature to restore the gold standard or peg the pound because the underlying disequilibriums still remained. Interest rates however had fallen and should remain low, whereas credit should be sufficiently easy to be "adequate to meet the requirements of expanding trade and industry provided that no speculative movements occur." With respect to the conference itself a penciled Treasury note said the interrelationship of Empire currencies was a "minor" question. The author urged that there should be no discussion of the price level and stabilization. "All the economic and currency experts will want to propose every kind of scheme. If the matter is referred to them we shall have nearly as many recommendations as there are experts, with a very unsettling effect on sterling and on confidence."¹³

At Ottawa in summer 1932 Chamberlain hewed to the Treasury line and got his own way to a large extent. With him in Ottawa were Sir Frederick Phillips from the Treasury and R. N. Kershaw, the Bank's expert on Empire monetary matters. As Hopkins and the Bank had urged, he was able to avoid any commitment to the gold standard, exchange stabilization, or inflationary finance. Yet he was able to convince the Dominions and India that the United Kingdom was conveniently committed to cheap money and to credit expansion for legitimate commercial purposes. Finally he was able to convert the Dominions concerned with low agricultural prices into acquiescence in his own projects of commodity control.

The conference delegated monetary and financial questions to a special committee. On July 29 Chamberlain explained what the United Kingdom would and would not do. Prices should rise, he said. But disequilibriums between production and consumption were as much to blame for the existing situation as any monetary policy. Reparations had caused further problems, as had the drying up of investment capital. He announced: "it cannot be contended that the world can be put right or even that prices can be restored merely by an alteration of the monetary factor." The conferees could do nothing for the prices of commodities in which there was a world market. When Britain was the principal buyer, Chamberlain urged, the delegates should consider regulating their exports. As for stabilization, there was no point in discussing it. The

flows of hot money were so great that even Britain's Exchange Equalisation Account could not be sure of stabilizing the exchanges, much less pegging them permanently at some definite level. Britain would continue to keep credit plentiful and cheap. But there should be no "rash experiments in monetary policy."¹⁴ In response to pressure from Dominion delegates, especially from S. M. Bruce of Australia, Chamberlain later went so far as to say his government was "confident that the efforts which have successfully brought about the present favourable monetary conditions can and will, unless unforeseen difficulties arise, be continued."¹⁵ Later he told his own delegation that 'it was unlikely that any very startling recommendations would result from the deliberations of the Committee . . . As the Delegations were not agreed on the major issues, their report would contain no controversial matters, and would in all probability be unanimous."¹⁶

It has been said that the Ottawa Conference committee on monetary questions was meaningless.¹⁷ In the context of the conference proceedings that adjective is certainly appropriate; the conference was not about money, and it took no binding decisions on exchange rates. Nevertheless, though at the time the committee report was little more than Chamberlain's device to head off the wilder inflationary proposals and to keep the Empire quiet, once embedded in the conference conclusions the report acquired a very considerable importance. On the one hand Britain could and did use it as a public statement of its own policies with respect to cheap money, low interest rates, and easy credit for legitimate commercial purposes; on the other hand it could and did serve to define Britain's policy with respect to gold and the gold standard.

Neither the committee nor the conference said anything about the desirability of stabilizing sterling relative to gold. It was merely observed that the United Kingdom would try to offset speculative movements in the price of sterling, and that it would be valuable if Empire countries could maintain stable exchange rates on a sterling basis. Nor was anything said about exchange reserves, London credits, or exchange controls. It was higher prices, Chamberlain and the delegates agreed, that would help to stabilize intrainperial exchange rates. Indeed, Chamberlain made every effort to convert the monetary discussion into a program for price raising through production control.

With respect to the gold standard itself, Chamberlain recognized that Canada and South Africa were in favor of gold. But he explained, "We must make it clear that we have no intention of returning to the gold standard unless we can be thoroughly assured that a remedy has been found for the maladjustments which led to the breakdown of that standard last year . . . Before we change our present basis we must be sure

that the change can be maintained and that we shall not have to do our work all over again in a few years' time."¹⁸ The committee report followed the same course. Ultimately, it declared, there should be a "satisfactory international standard." This should not only keep exchange rates stable but should ensure that finance and trade would work smoothly. Such a standard could exist only if there were agreement among the "great trading nations of the world" and only after "several conditions precedent" had been attained: higher commodity prices and an "adjustment of the factors political, economic, financial, and monetary which have caused the breakdown of the gold standard in many countries, and which, if not adjusted, would inevitably lead to another breakdown of whatever international standard may be adopted." Furthermore, the new arrangements, when and if they were introduced, should be designed to avoid "wide fluctuations in the standard of value."¹⁹

With respect to gold and the stabilization of exchanges Britain and the Empire had now defined a policy. But it was still really Britain's policy; South Africa still clung to the full gold standard, and Canada was operating a somewhat unclean float with her eyes fixed not on sterling but on the U.S. dollar. As for the rupee, though the Indian currency was stabilized on sterling both Indian opinion and Indian officials wished it were not. In the next three chapters we follow developments in these three great Empire countries.